

NTA and Monthly Update – June 2017

Company at a Glance

ASX Code	ALF
Fund Size	AU\$342.5m
Fund Strategy	Variable Beta
Share Price	\$1.205
Shares on Issue	272.5m
Dividend (HY17 Interim)	4 cents
Dividend Yield (annualised)	7.0%

Net Tangible Asset (NTA) Backing

	May 17	Jun 17
NTA Before Tax	\$1.27	\$1.26
NTA After Tax	\$1.28	\$1.27

Gross Portfolio Structure

Long Exposure	119.9%	130.9%
Short Exposure	-121.4%	-131.0%
Gross Exposure	241.3%	261.9%
Cash	101.5%	100.1%

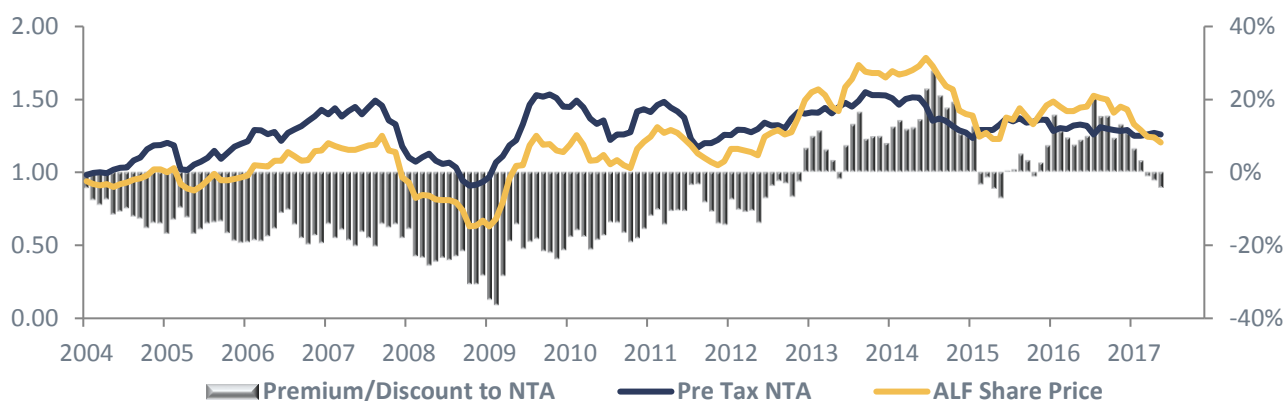
ALF Performance

	1 Mth	6 Mths	1 Yr	3 Yrs (pa)	5 Yrs (pa)	7 yrs (pa)	S.I. (pa)
Portfolio Return (net)	-0.5%	0.7%	2.0%	3.1%	12.3%	11.5%	13.0%
All Ords Accum Index	0.3%	2.9%	13.1%	6.8%	11.6%	8.8%	8.8%
Outperformance (net)	-0.8%	-2.2%	-11.1%	-3.7%	0.7%	2.7%	4.2%

Net Equity Exposure



Premium/Discount to NTA History



Month in Review

With consensus between central bankers forming around a move towards tighter monetary policy settings, malaise in share markets here and abroad gave way to volatility in June, with most major share indices posting falls. Having led the way in the effort to normalise interest rates, the US Federal Reserve announced its third rate hike in 6 months, finding comfort from continued strength in the performance of the domestic economy. European and Canadian markets proved more skittish at the prospect of rising rates, with sharp increases in local bond yields signalling an ominous warning for investors in shares of potential for market falls once this policy shift begins in earnest.

The Australian share market was held back by a raft of earnings downgrades and weak performance from bond proxies in the REIT and Utilities sectors. The domestic economy continues to grind along, showing some modest improvement in the labour market and in spite of elevated household debt levels and a cooling residential property sector.

The portfolio fell in value by 0.5% after all fees, trailing the benchmark All Ordinaries Accumulation index which rose by 0.3% in the month. Over the course of the year to June 30, the Fund's international exposures made a solid positive contribution to performance while the domestic portfolio was largely flat. The Fund's neutral exposure settings have been maintained, with markets here and abroad looking fully valued. A long bias to the financial sector worked well in the month, while exposures in the mining and consumer discretionary sectors were the biggest detractors.

The extent to which Central Banks are coordinated - if not in practice then at least in intent – was reflected in the minutes of meetings and resulting commentary through the month. Specifically, the minutes from the UK Monetary Policy Committee showed three of the eight members voted to raise interest rates from 25bps to 50bps at its June meeting, an increase from just one of eight voting for a rate rise at the May meeting. Secondly, the minutes from the June meeting of the ECB Governing Council showed that officials discussed whether to end the Central Bank's commitment to increase the rate of bond purchases if the European economy deteriorated. Finally, the US FOMC raised its Federal Funds Target rate 25bps to a range of 100-125bps.

The Fund's financials positions performed well in June. The domestic portfolio benefitted from a long position in Henderson Group, which completed its merger with Janus, and a short position in QBE Group which issued an earnings downgrade. Internationally, a long position in Allied Irish Bank made a solid contribution, following its recent re-IPO, as did an investment in Wells Fargo which exceeded market expectations in the US Fed's annual Comprehensive Capital Analysis and Review (CCAR). The Fund's long bias in financials was reduced towards the end of the month.

Hawkish overtones from the head of the ECB and a stronger EURO drove a rotation out of defensive sectors like healthcare, into more inflation/interest rate sensitive exposures. After stellar performance in the prior 3 months, European healthcare names bore the brunt of this rotation. US biotechnology shares caught a strong bid following a spate of positive clinical trial results, softening in the rhetoric around drug pricing out of Washington DC and increased speculation of M&A in the sector. Notwithstanding the softer government rhetoric, we maintain that the structural drivers of drug pricing pressure are yet to have their full impact.

Prices of Australian healthcare companies continue to push higher, with valuations now reaching extreme levels. Sector heavyweights such as CSL, Cochlear, Resmed and Sonic Healthcare; all hit record highs in June with most valuation metrics pushing well above 1x standard deviation versus historic levels. This momentum is being supported by a range of factors, including capital inflows as investors rotate out of financial shares and positioning for a weaker Australian dollar. Domestic positions detracted from performance in June, with a solid contribution from a core investment Ramsay Healthcare offset by losses in the short portfolio. International positions fared better, with positive contributions from European shorts, as well as investments in Nevro, Celgene and Allergan.

Having almost singularly led the US share market higher in recent times, the technology sector suffered its worst month in nearly 2 years, with the US technology index down 3%. Most of the weakness was seen in the semiconductor sector, which fell by 5%, while internet and software companies mostly recovered losses from

earlier in the month. Hardware names felt the pressure of concerns that this year's iPhone release in September is facing supply challenges and may be delayed. June was also a month to forget for the global telco sector which fell by 4% as global bond yields rallied. Consolidation in the US now seems to be on hold for the time being, while regulation in Europe has become more heavy-handed.

Our TMT portfolio is well hedged and remained resilient during the month, reporting flat performance through this volatility. Domestically, Fairfax detracted from performance as both potential suitors failed to submit bids by the deadline. Globally, our short positions in European broadcasters performed well, helped by price falls due to the continued dislocation of TV advertising revenues from macroeconomic conditions. A short in STMicroelectronics also contributed strongly.

Global consumer staples shares declined in June for the first time this year, while their Australian peers extended a recent run of weakness. The more economically sensitive consumer discretionary shares were largely flat in both global and domestic markets. A new long position was established during the month in Bapcor (aftermarket auto-parts) following the market sell-off, while the company digests its recent acquisition of Hellaby's. An investment in US supermarket Kroger was sold down in response to increasing competitive intensity in the US grocery market while profits were taken in domestic wagering company Tabcorp, with the price having met our assessment of fair value.

In aggregate, consumer positions detracted from performance over the month, in particular US investments in Kroger and O'Reilly Automotive; as any sign of trading weakness in US consumer stocks was assumed by the market to imply permanent disruption by Amazon. Strong returns were generated from short positions in US companies Campbell Soup and Best Buy. Australian positions were largely unchanged.

Industrial shares were flat in June – valuations are high by historical standards, however leading economic indicators of the industrial sector continued to show reasonable strength in the US and Europe, with China maintaining momentum. Given the strength of the Euro, European industrials with large offshore businesses underperformed their US peers. Infrastructure was a positive contributor, with the funds appropriately positioned for a sell-off on rising in bond yields, while capital goods and transport were slight detractors. The Fund remains fully hedged, with investments in higher quality companies benefitting from restructuring and themes such as industrial internet, balanced by short positions in more cyclical shares, on high valuations and carrying risk of disappointment.

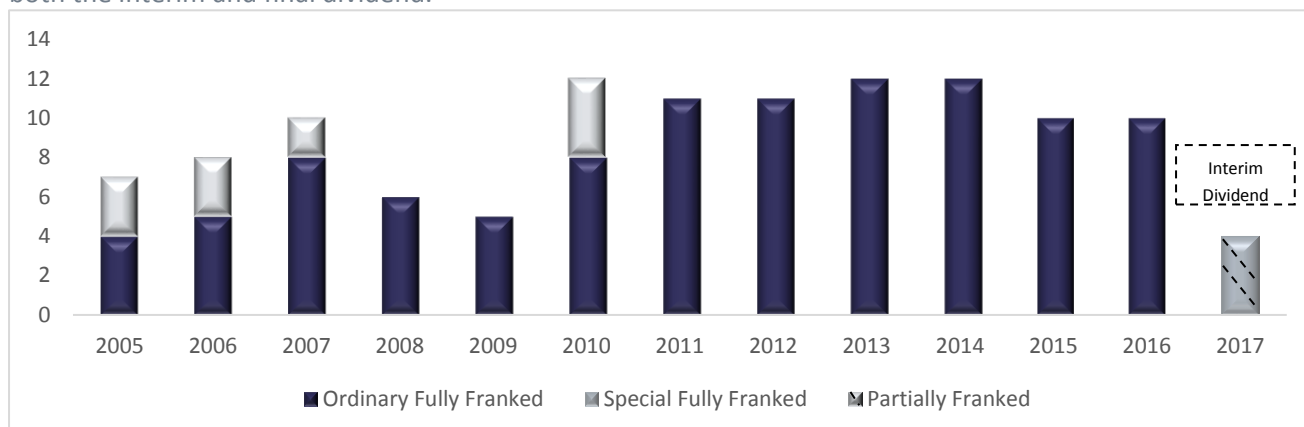
Mining shares continued their recent declines before staging a rally in the second half of the month. Chinese Government news outlet Xinhua reported the need for "loose credit conditions", while the Chinese Ministry of Finance announced it would increase liquidity in the bond market. The oil price fell as focus shifted from OPEC optimism to rising US inventories, while the gold price dropped in response to central bank commentary.

We reduced our short exposure in mining through the month, largely via an increased holding in BHP Billiton. The company announced the appointment of new Chairman, Ken MacKenzie, who comes with an impeccable track-record at industrial company Amcor. We have already seen two broker upgrades since the appointment which has assisted short term performance. We remain balanced in our Energy portfolio but used recent weakness to initiate an investment in Origin Energy. Origin is embarking on a split of upstream assets which we believe will be sold to help reduce the high debt levels of the company. The high-quality energy markets business, and their east coast LNG project will remain.

The Basic Industries portfolio detracted from performance in the month as the Mining sector rallied. This was compounded by impacts on a core investment in Independence Group from a cautious progress update at its key development mine - Nova. We were well positioned for the sell-off in oil however, with our short in oil supermajor Total SA, contributing to performance.

Dividend History

The Board is committed to paying an increasing stream of fully franked dividends to shareholders, provided the Company has sufficient profit reserves and franking credits and it is within prudent business practices. Dividends are paid on a six-monthly basis and the dividend reinvestment plan is available to shareholders for both the interim and final dividend.



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